

# Self Canceling Installment Note

Essentials 2018

Self Canceling Installment Note (SCIN) is an effective method to transfer assets to subsequent generations with minimal gift and/or estate tax costs. A SCIN is often used when transferring highly appreciating or income producing assets to subsequent generations.

## How A Self Canceling Installment Loan Works

1. An asset is sold to buyer for a note. The note bears a rate equal to the applicable federal rate based on the term of the note. A risk premium is added either to the interest rate or the sales price.
2. Seller receives payments and reports gain spread over the term of the note.
3. If seller dies before the final payment, the note is canceled.
4. If buyer dies before the final payment, the buyer's estate must continue making payments until note is satisfied. (A life insurance policy on the buyer can cover the risk of non-payment.)

## Considerations

- The client sells the asset(s) to a trust or individual in exchange for an installment note payable over a specified period of time.
- The seller will generally recognize gain over the term of years. The installment sale rules are very complex.
- The assets sold will hopefully provide sufficient income to cover the debt service.
- The note term must be less than the life expectancy of the seller and will contain a self-canceling clause in the event of seller's death.
- The note must bear an adequate rate of interest based on the note's duration – based on the applicable federal rate (short-term, mid-term, or long-term). The SCIN interest rate must contain a risk premium to compensate in the event of an early death or the face amount must include a risk premium, or a combination
- If the risk premium is not sufficient, then the transaction will be treated as a part-sale, part-gift transfer.

## Essentially

SCINs can be an effective way to transfer assets to subsequent generations at little to no gift and/or estate tax costs.

